DOW THEORY LETTERS INC.

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36 Letters per Year—$60.00 Annually

Registered with the Securities Exchange Commission

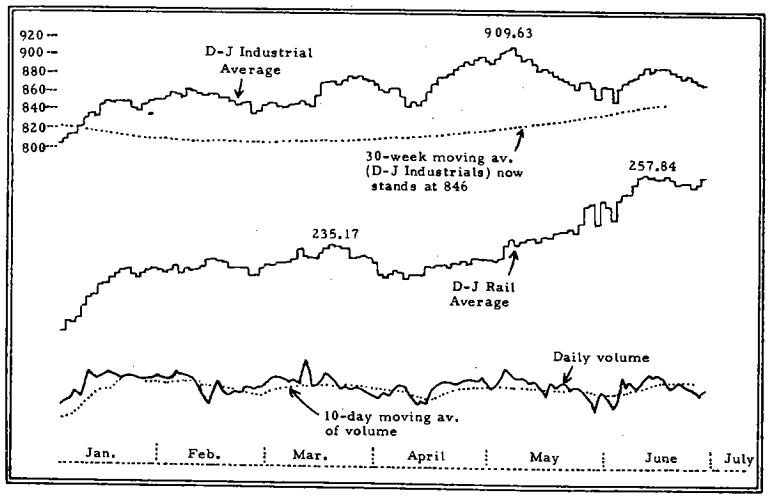
June 30, 1967 Letter 362

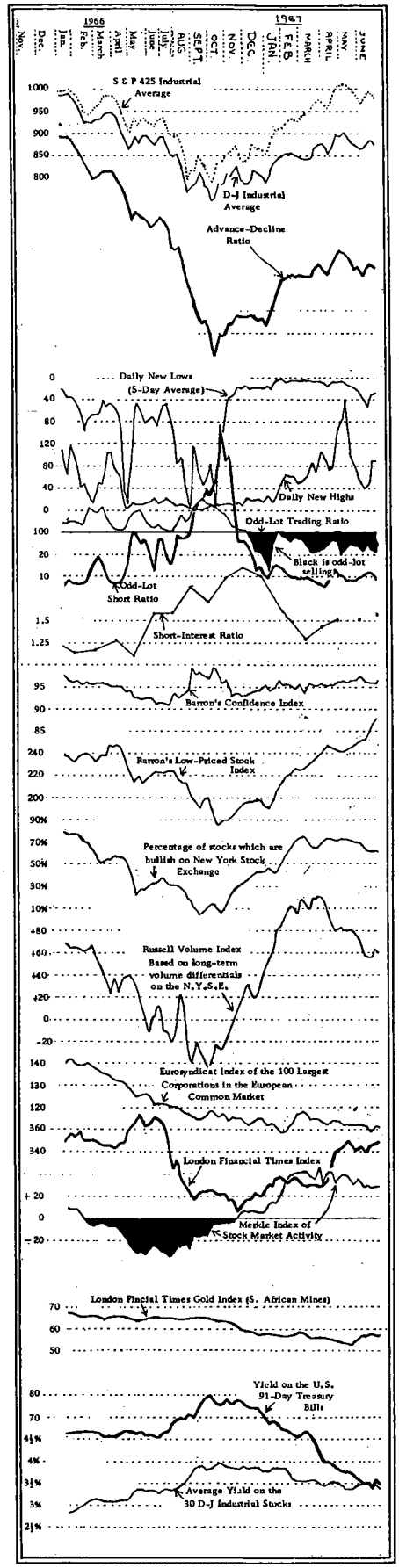
THE MARKET: Over any extended period of time, the trend is set by investment money. Historically, as I have stressed here so many times, it is the trend of the blue-chips, the General Motors and the duPonts and the General Electrics, that sets the overall long-term trend of the market. Of course there are periodic speculative outbursts. These are the intermediate periods in which low-priced and certain fashionable issues grab the spotlight. But in the end it is the investment-grade issues and the investment money that sets the main trend.

We saw a brief abortive period during early 1966 when the speculative low-priced stocks were running wild, even while the high-grade stocks and the D-J Industrials were sinking. In the end, the investment issues and the investment money proved the strongest force in Wall Street. By October, 1966, the entire market was in shambles.

Again during most of the 1966-67 bear market recovery the speculative issues moved to the fore. Nobody has waxed poetic about General Motors or Westinghouse during 1967. It was all Sperry Rand, Gulf & Western and Avco. This type of action has always resulted in a dangerous climate for the market; but when it occurs during a bear market rally I believe it is doubly dangerous. In my opinion, a great amount of distribution has taken place during 1967, mostly in investment-grade issues. When the distribution is over, the high-grade issues will crack as they did in 1966. Following that the speculative segment will cave-in with little or no signs of support (as per 1966). But because the 1966-67 bear market retracement has been well above the average in duration, extent and speculative intensity, I would expect the ultimate decline to be more drastic and much more damaging than anything seen during 1966.

There seems to be a general misconception about secondary corrections during bear markets. Many analysts (who have not studied their subject) were unduly impressed by the 2/3 recovery in Industrials during 1966-67. Some even mouthed nonsense to the effect that "anything above a 2/3 recovery would constitute a 'bull signal' under the Dow Theory." Nothing could be further from the truth. Robert Rhea did much of the original work on exact computations of market swings. He found that about half of all bear market rallies fell within the "standard" 1/3 to 2/3 retracement limits, while the other 50% of bear market corrections ran either to less than 1/3 retracements or to better than 2/3 corrections. In fact, some bear rallies have taken one or the other Average back above the old highs,




1966
1967
S & P 425 Industrial Average
D-J Industrial Average
Advance-Decline Ratio
Daily New Lows (5-Day Average)
Daily New Highs
Odd-Lot Trading Ratio
Block is odd-lot selling
Odd-Lot Short Ratio
Short-Interest Ratio
Barron's Confidence Index
Barron's Low-Priced Stock Index
Percentage of stocks which are bullish on New York Stock Exchange
Russell Volume Index Based on long-term volume differentials on the N.Y.S.E.
Eurosyndicat Index of the 100 Largest Corporations in the European Common Market
London Financial Times Index
Merkle Index of Stock Market Activity
London Fincial Times Gold Index (S. African Mines)
Yield on the U.S. 91-Day Treasury Bills
Average Yield on the 30 D-J Industrial Stocks

 so that the percentage of correction in a single Average would then have been better than 100%.

To get back to specifics, it appears to me that this market is slowly but relentlessly running out of technical strength. The movement of the highest-grade investment segments of Wall Street are making no progress; the 40-Bonds and Utilities have been registering a long string of new 1967 lows. The Industrials and Rails are now faltering, and only the most speculative elements of the market are still pushing higher (for example, the DJI gave up over 7 points last week in the face of a new high in Barron's Low-Priced Stock Index). I repeat, this type of action is not healthy; it was last seen in early 1966 just before the first phase of this primary bear market.

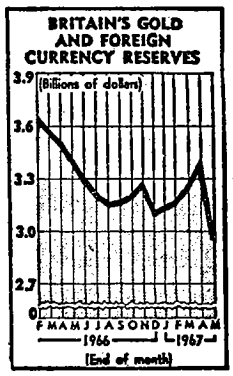
My group studies are showing deterioration, with only 44 of the 89 Standard & Poor stock groups now acting better than the S & P 500 Stock Average. In the past when this occurred it has meant trouble for the entire market. I am currently going over my group momentum studies (I use three separate methods of group studies), and I intend to present a complete rundown of these methods in the next Letter. I believe subscribers will find these analyses most useful and informative.

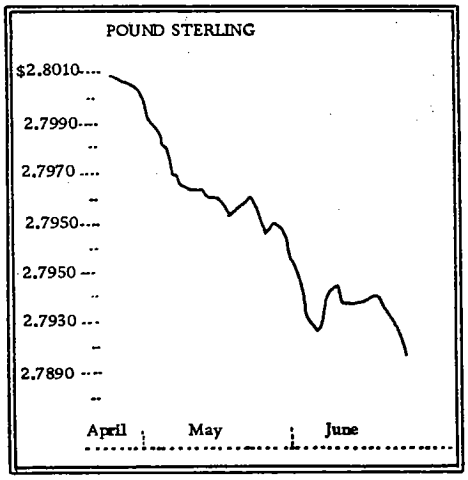
I want to warn subscribers again about the dangers of the bear market. Our administration and its various agencies have been indulging in one of the most massive manipulative efforts in history in an attempt to hold back the primary bear forces that lurk under this market and under this economy. Free reserves have been pushed way up by the Federal Reserve; that same agency has been attempting to support the long-term bond market while also providing massive support to the short-term bill market. Huge Government contracts have been let out, Great Society programs have been strenuously pushed in the face of fantastically expensive war efforts, pronouncements by Governmental leaders have been almost uniformly bullish despite many signs of economic stress and strain.

In fact, I doubt if there has been a period in history in which a Government has so recklessly butted its head against the natural primary forces which were amassed against it. In the end, I believe the primary force of the market and the economy will make shambles of the bulls in Government and the bulls on Wall Street. I would guess that perhaps most of the steam is already out of the current stock market rally. It was this rally that reflected the sum total of all the manipulative Governmental forces seeking frantically to push "everything" higher. Yet, so far, at the May 8 closing, the Dow Industrials have been able to retrace only 65% of the ground lost during the 1966 decline. The Rails retraced 83% of their decline, while Utilities were sluggish during the whole rally, and at present are not far from their bear market lows.

I want to remind subscribers that in the past when a primary movement was extended or held back, the ultimate resumption of the primary trend was more drastic and more extended than would otherwise be the case. Therefore, I feel that subscribers should be prepared for a drastic downward movement when this rally spends itself. If I had to bet, I would wager that the primary bear forces will take hold between now and July or August (with the possibility that they are already exerting their downward pressure as of this writing).

DOWN GOES THE POUND: Adding to the potential trouble spots that dot the political and economic world, the pound sterling has quietly dropped over 100 points from its Spring high of $28.015 touched in April, 1967. At present the pound is around or below its old low at $27.900. Thus pressure is increasing on sterling. The only difference this time (versus the last weakness of the pound in 1965-66) being that this time nobody seems to be noticing the trouble.





What has happened? For one thing there was a huge build-up of Euro-dollars during 1965-66 as a result of loans to England. These loans were borrowed by American firms, but currently they are being run off. The Americans simply don't want or need the funds. Secondly, the British have decided to try to "reflate" their sagging economy, and such action is bound to raise doubts again about British trade-balance intentions. Next month 6 million British workers are due to get pay raises. Imports are rising, and the export picture is looking cloudy. The whole balance-of-payments picture out of Britain continues to look poor.

The Mid-East crisis has put further strain on the pound. England may now have to pay vastly more for oil, oil which is being denied it by the Arabs. Finally, it is almost certain that Britain will have to borrow again on loans which were paid off in the more optimistic atmosphere of early 1967. Such a payment, for instance, was the prepayment of part of the I.M.F. loan, a loan which comes due again this December.

The acconpanying chart shows the path of the spot price of the pound since April. It is telling the story better than anything I could include here. Pressure on the pound, if it continues, will soon put the gold stocks in the limelight. Any British devaluation would almost certainly set off devaluations in the two gold-producing nations of the Free World, Canada and South Africa. The S. African rand, for example, is directly convertible into pounds, there being two rands to a pound.

A great many of my subscribers have taken my advice and are hedging their positions by holding 10% to 15% of their assets in Canandian and S. African gold shares. Many of the S. African shares are now providing yields of up to 9%. They are quoted daily in the "Foreign Securities" section of the Wall Street Journal. I include at right the latest statistics on leading S. African gold mines as published in Standard & Poor's "Foreign Securities Survey." Note particularly the growth in Western Deep Levels, destined to be the world's largest gold producer.

Year ended	a Tons milled	b Gold revenues	b Work'g profits	Per Amer. Sh. ($) Earns.	c Div.
BLYVOORUITZICHT					
6-30-66----	1769	38.9	20.7	0.56	0.31
6-30-65----	1753	38.5	20.5	0.61	0.32
6-30-64----	1768	38.9	23.1	0.52	0.34
Shares outstanding: 24,000,000.					
FREE STATE GEDULD					
9-30-66----	1864	68.9	49.5	2.13	1.50
9-30-65----	1831	68.5	50.0	2.07	1.53
9-30-64----	1688	62.2	44.5	1.96	1.33
Shares outstanding: 10,000,000.					
PRESIDENT BRAND					
9-30-66----	2490	57.4	35.2	1.24	0.93
9-30-65----	2484	57.7	35.9	1.26	0.91
9-30-64----	2205	50.9	32.2	1.30	0.88
Shares outstanding: 14,040,000					
WEST DRIEFONTEIN					
6-30-66----	2766	81.2	50.7	1.79	1.14
6-30-65----	2705	75.8	47.8	1.74	0.96
6-30-64----	2604	67.6	41.8	1.67	0.83
Shares outstanding: 14,082,160.					
WESTERN DEEP LEVELS					
12-31-66----	2965	52.3	26.6	1.06	f0.40
12-31-65----	2742	41.2	19.7	e0.76	f0.37
12-31-64----	2409	30.0	12.5	e0.47	f0.27
Shares outstanding: 25,000,000.					
WESTERN HOLDINGS					
9-30-66----	2700	68.6	45.5	2.52	2.00
9-30-65----	2683	69.2	47.4	2.80	2.04
9-30-64----	2446	62.2	42.7	2.37	1.75
Shares outstanding: 7,496,376.					

a Thousands. b $ millions. c After 7½% South African withholding tax until 8-17-66. 10% thereafter: calendar years. e On total shares outstanding. f Paid on "A" shares; initial $0.054 dividend on "B" shares paid in August, 1966.

ANNOUNCEMENT: I believe I have solved a two-pronged problem, and with this mailing I will let subscribers in on the secret. My first problem was that I was being squeezed by price rises; rises in printing, postage, labor. Dow Theory Letters has been one of the lowest-priced investment services in the business; it has cost one-third to one-half the price of most other leading services. Raising the price of the service does go against my grain. I simply have not wanted to jump on the inflation bandwagon. Nevertheless, my cost problem will not evaporate via my wishes. I decided that a price of $60 per year, $35 semi-annually, was still reasonable when compared with the price of other services. I took an average of 12 leading services which I receive here, and that average price was $115 per year. At my new price of $60 annually, I offer Dow Theory Letters at about half the price of the 12 other services.

Next, I wanted to give my subscribers something more in the face of the new price rise. If they are going to pay more, I want to give them more regardless of printing, salary and mailing expenses. And I have hoped to give something which I felt was worth considerably more than the additional price increase. In other words, my goal was to make Dow Theory Letters a bigger bargain at the new price than at the old price.

I believe I have done that. In the course of the past five years, I have noted an increasing sophistication among my readers financial affairs. They want to know everything— and I don't blame them. The bulk of inquiries I have received here have to do with "what's going on in the business world, the money world, the bank-credit world." It is a fact that many subscribers of mine subscribe to other publications which deal with such subjects as business or bank credit money. I have wanted to give subscribers the whole picture in one easily-read package. Furthermore, I feel that with a primary bear market in force it is more important than ever to provide readers with the reasons and facts behind the events, events which are almost guaranteed to affect our lives and our financial fortunes over the coming years.

Therefore, I have, with this mailing, started something which I have wanted to start for a long time. It is a new service dealing with the financial outlook for investors and businessmen. The service is being edited by a long-time friend of mine, Michael Holzman. Mr. Holzman has the quality of incisiveness and clarity. He is a brilliant, highly-competent observer of the financial scene, and I feel that in every way Mr. Holzman is qualified to write this new report.

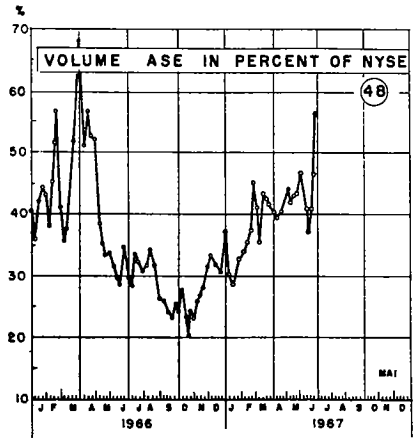
From here on, the Economic Trends Letter will be included with each mailing of Dow Theory Letters. I have already received inquiries regarding whether the new report will be sold separately. The answer is no. For purposes of simplified records and cost-control, the Economic Trends Letter will only be distributed to readers of Dow Theory Letters.

Now, a final comment. Over the next two weeks I will accept advance subscriptions to both services from current subscribers at the old price of $50 per year. Therefore, if you wish to extend your current subscription one or two or three years beyond its present expiration date, please send me a check for the proper amount and your subscription will be extended accordingly.

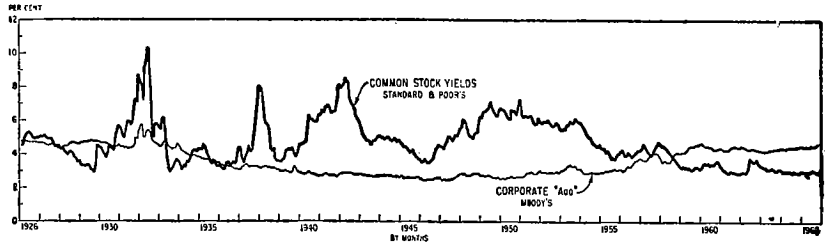
BEAR MARKET NOTES: Federal Reserve Board Chairman Martin stated on June 27 that he wanted a prompt tax increase. The reason: to stem inflationary pressures. But it has already been estimated that corporate tax receipts to the Government are slated to drop at least $4 billions this year. A second reason could be that Mr. Martin is afraid of the coming budget deficit and wants the Government to take in more money. Finally, it would appear that a behind the scenes deal was made whereby the Fed would open the money gates if the Administration would agree to a large tax increase. The money gates are open wide, thinks Mr. Martin, and his demand for the tax increase could well be a warning to the Administration to start moving on taxes.....

The European so-called "Group of 10" has written off the U.S.-British dream of a new "paper gold currency." The Group has decided that if more liquidity is needed, drawing rights from the I.M.F. will be increased. The leading powers in Europe have

a fat position in gold. The U.S. was dreaming when it thought it could ask them to substitute paper for gold. It was tantamount to asking France, Germany, Belgium, Holland, etc. to bet against their own investment position.....



Last week the volume on the Amex ran to 58% of that on the N.Y.S.E., the fourth highest such ratio on record (see accompanying chart courtesy of Merrill Analysis, Box 228, Chappaqua, N.Y.). Despite this frantic speculation by crapshooters on the Junior Exchange, the Dow keeps slipping. The ultimate decline, following this period of frenzied speculation and distribution, should be a "hair-curler."



By the middle of last week, the negative spread between the yield on the S & P 500 Stock Average and the yield on the S & P "Aaa" Bond Average rose to 228 basis points. This was the third week running of historic yield-spread records. With stocks in high territory (providing low yields) and bonds declining, nothing like the current yield spread in favor of high-grade bonds has ever been seen. To say that the situation is dangerous is to put it very mildly indeed (see chart above).

Speaking of bonds, Wall Street is blinking its eyes at what is going on. By last week top-grade corporate bonds were touching the 6% yield level, 17 Treasury bonds were yielding over 5% with some as high as 5.25%, and average yields on tax-exempt municipal bonds had risen to 4%. Said the editor of the authoritative Weekly Bond Buyer, "There are senses of foreboding on the Street that do not lift, and if so little is written about them or heard about them beyond the canyons of the Street, it is because these forebodings are intermingled with an odd sense of fatalism; after all it does no good, on a raft headed for Niagara Falls, to jump into the current."

At the close on June 26, the bellwether of the long-term U.S. Treasury bond market, the 4¼ of 1987-92 (see chart in last Letter) closed at an historic low of 88.0 to yield 5.06%. A day before the D-J 40-Bond Average closed at 80.29 for a new 1967 low. The 80.29 low was exactly 31¢ above the 1966 low, which in turn was the lowest level for the 40-Bonds in 33 years. In case subscribers fail to grasp the point, I want them to understand that this bond market is teetering on the edge. It is just this side of chaos. Perhaps the most ominous part of it is that the Treasury bonds have been toppling to new lows in the face of heavy Federal Reserve buying support. To that extent the bond market is considerably weaker than it was last year.....

The ammunition used by the bulls in referring to "this new bull market" was that business was going to boom starting with the third quarter of 1967. Now the pick-up is being shifted to the fourth quarter of 1967 or early 1968. Meanwhile, the market has to deal with what it may be like if high interest rates prevail for the remainder of 1967. The market also has to deal with the little matter of second quarter earning—which will be trickling in shortly. According to Alan Abelson of Barron's (June 26), second quarter profits are ".....likely to range from generally disappointing to downright shocking." Newsweek (June 27) notes that the few quarterly statements which they have seen for the quarter ending April 30 indicate that profits will be down as much as 32%.....

In case you are taken with the skill of Government experts, here are some revisions on the January forecast of the Council of Economic Advisors. GNP will be $780 billion instead of the original $787 billion estimate. Corporate profits are to be $78 billion instead of $83 billion. Plant and equipment expenditures are to be $61 billion instead of $63 billion. The FRB Production Index will not get back to last December's 159, although in January it was considered a sure thing to better 1966's record in 1967.

STOCKS: The speculative leaders of the whole rise from 1962 to 1966, and to some extent the bear rally of 1966-67 have been the airlines. Now that speculative leadership is beginning to crumble. At right (courtesy of Quote Digest, 110 N. Lorraine, Wichita, Kansas) are weekly charts of three representative airlines. Head-and-shoulders formations have formed in all three, and it would appear that this high-flying group is in the process of coming down to earth. My bet is that the airlines have seen their highs for many years to come. They represented the spearpoint of the frenzy on the upside for the past five years. Their downturn indicated a slow subsiding of the froth. I doubt that a new speculative group will be found to take their place.